SOAH DOCKET NO. 473-21-0538

PUC DOCKET NO. 51415

PUBLIC UTILITY COMMISSION OF TEXAS

APPLICATION OF

SOUTHWESTERN ELECTRIC POWER COMPANY

FOR AUTHORITY TO CHANGE RATES

REBUTTAL TESTIMONY OF

RENEE V. HAWKINS

FOR

SOUTHWESTERN ELECTRIC POWER COMPANY

APRIL 23, 2021

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I. INTRODUCTION

Q. PLEASE STATE YOUR NAME, POSITION, AND BUSINESS ADDRESS.

A. My name is Renee V. Hawkins. My current position is Managing Director of Corporate Finance for American Electric Power Company, Inc. (AEP). AEP is the parent company of Southwestern Electric Power Company (SWEPCO or the Company). My business address is 1 Riverside Plaza, Columbus, Ohio 43215.

Q. DID YOU FILE DIRECT TESTIMONY IN THIS CASE?

A. Yes.

II. PURPOSE OF REBUTTAL TESTIMONY

Q. WHAT IS THE PURPOSE OF YOUR REBUTTAL TESTIMONY?

A. My rebuttal testimony responds to the direct testimony of Staff of the Public Utility Commission of Texas (PUCT or Commission) witness Mark Filarowicz (Staff). More specifically, I address Staff's recommendation to reduce SWEPCO's cost of debt from 4.18% to 4.08%, and the recommendation that the Commission impose or require certain financial protective measures (Ring-Fencing) on SWEPCO.

Q. PLEASE SUMMARIZE YOUR REBUTTAL TESTIMONY.

A. I continue to recommend that the Commission approve the Company's proposed 4.18% cost of long-term debt. The Company's requested cost of debt is the actual cost of debt for the test year. Staff's recommended adjustment is not based on a known and measurable change and does not consider the Company's long-term debt requirements. Moreover, the other witnesses in this rate case that address cost of capital issues adopt the Company's proposed 4.18% cost of debt in their own cost of capital recommendations.[1]

With respect to ring-fencing, Staff's recommendations are overreaching and unnecessary to protect SWEPCO and its customers.

III. COST OF DEBT

Q. WHAT DOES STAFF RECOMMEND FOR THE COMPANY'S COST OF DEBT?

A. On pages 8 and 31 of his direct testimony, Mr. Filarowicz recommends that the Company's cost of debt be adjusted down from 4.18% to 4.08%.

Q. WHY DOES STAFF MAKE THIS RECOMMENDED ADJUSTMENT?

A. Staff recommends removing the annual effects of the Series I Hedge Loss, which is being amortized from February 2012 through January 2022 (ten years) because customers have already paid 93% of the amortized loss and (in Staff's opinion) it would be inappropriate to set future rates on an event that occurred in 2012. On page 31 of his direct testimony, Mr. Filarowicz states that the Series I Hedge Loss will be fully amortized in January 2021. But, it will actually be fully amortized as of January 31, 2022, as indicated in the Company's response to Commission Staff's Sixth Request for Information at 14, Staff 6-12 (Dec. 21, 2020). The rates set in this case will go into effect as of March 18, 2021. Thus, the Series I Hedge Loss amortization occurs during both the test year and the period when new rates are in effect.

[1] See Direct Testimony of Michael P. Gorman, on behalf of Texas Industrial Energy Consumers, Exhibit MPG-1; Direct Testimony of J. Randall Woolridge, on behalf of Cities Advocating Reasonable Deregulation, page 4 (Table 2 – CARD Rate of Return Recommendation); and Direct Testimony of Lisa V. Perry, on behalf of Walmart Inc., Exhibit LVP-2.

Q. DO YOU AGREE WITH STAFF'S RECOMMENDED ADJUSTMENT TO THE COMPANY'S COST OF DEBT?

A. No. The Company's requested cost of debt of 4.18% is reasonable and consistent with 16 Tex. Admin. Code § 25.231(c)(2)(F). Staff's recommended adjustment based on the removal of the Series I Hedge Loss amortization does not consider the impacts on all aspects of SWEPCO's operations. Staff recommends pulling one item out of the cost of debt without considering any other changes that will or may occur between now and February 2022. Moreover, the Company's requested cost of debt conforms to the use of a test year ended March 31, 2020. SWEPCO's rate base and weighted average cost of capital is matched to the test year end date of March 31, 2020. This approach provides a fair return on investment. It would be imprudent and unreasonable to adjust cost of debt for expected changes almost two years after the test year end. Even if it were prudent to do so, you would also have to consider anticipated rate base increases between March 2020 and February 2022. It would be impossible to anticipate all of the numerous changes impacting rate base that will occur prior to February 2022. That is why a test year is used to set future rates.

IV. RING-FENCING

Q. STAFF RECOMMENDS A SERIES OF RESTRICTIONS ON DIVIDENDS AND AFFILIATE TRANSACTIONS REFERRED TO AS RING-FENCING IN HIS TESTIMONY. DO YOU AGREE WITH THE RECOMMENDATIONS?

A. No. These restrictions are unnecessary and will add additional costs for SWEPCO's customers. It makes no sense for SWEPCO customers to incur the personnel, legal, financial, and other costs associated with ring-fencing when the risk(s) sought to be avoided by ring-fencing are not likely to occur for SWEPCO, its parent, or affiliates. Also, some of the proposed restrictions were specifically rejected by the Commission in Docket No. 49494 involving SWEPCO's affiliate, AEP Texas. In that case, the Commission analyzed the necessity of ring-fencing measures in the context of AEP Texas' corporate family and decided that many of the recommended measures were unnecessary. That same analysis holds true for SWEPCO.

Q. WHAT RESTRICTIONS ARE BEING PROPOSED?

A. The following restrictions are proposed on pages 44 and 45 of Staff Witness Filarowicz's direct testimony:

1. SWEPCO will work to ensure its credit ratings at S&P and Moody's remain at or above current ratings.[2]

2. SWEPCO will notify the Commission if its credit rating falls below investment grade.

3. If SWEPCO's issuer credit rating falls below investment grade, SWEPCO will not use that as justification for a higher regulatory ROE.

4. SWEPCO will ensure that it retains a stand-alone credit rating.

5. No cross-default provisions in credit agreements whereby a default by AEP or an affiliate would cause SWEPCO to default.

6. SWEPCO credit agreements will not include any financial covenants or rating agency triggers relating to any other entity.

7. SWEPCO will not share a credit facility with any unregulated affiliates.

8. No SWEPCO debt secured by non-SWEPCO assets.

9. SWEPCO assets will not be used to secure debt for another entity.

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[2] Staff mentions "dividends" in the title to Ring-Fencing Recommendation No. 1, but it is unclear from the description whether the recommendation includes a limitation on dividends tied to SWEPCO's credit rating.

10. SWEPCO will not hold out its credit as available to pay the debt of any AEP affiliates.

11. Except for access to the utility money pool and the use of shared assets governed by the Commission's affiliate rules, SWEPCO will not commingle assets.

12. SWEPCO will not transfer any material assets or facilities to an affiliate except on an arms-length basis in accordance with the Commission's affiliate standards.

13. Except for the utility money pool, SWEPCO will not lend money to or borrow money from AEP affiliates.

14. Without prior Commission approval, neither AEP nor its other affiliates will pledge SWEPCO assets for new debt that is dependent on SWEPCO's earnings or SWEPCO's stock price.

15. SWEPCO will not seek to recover from customers any costs resulting from an AEP or affiliate bankruptcy.

Staff further recommends that to the extent SWEPCO already complies with any of the above recommendations, the Commission should order SWEPCO to commit to continued compliance.

Q. DOES SWEPCO ALREADY COMPLY WITH THE TEXAS AFFILIATE RULES?

A. Yes. To the extent Staff's recommendations mirror the affiliate rules, it makes no sense that the Commission order SWEPCO to comply with regulations that it is already required to follow.

Q. DID STAFF PROVIDE ANY DIRECT EVIDENCE SUPPORTING THE NECESSITY OF FURTHER RESTRICTIONS ON SWEPCO?

A. No. Staff points to Energy Future Holdings and how the ring-fencing provisions adopted in Commission Docket No. 34077 effectively insulated Oncor Electric Delivery Company (Oncor) from bankruptcy. I am unaware of any other utility ownership structure that has been consistent with that for Oncor, but Staff essentially reasons that ring-fencing worked for that one unusual circumstance, so we should use it every time. Staff provides no specific analysis of AEP's structure, credit worthiness, or history other than to say that AEP is a big company with lots of affiliates.

Q. DOES STAFF MAKE A RECOMMENDATION REGARDING DIVIDEND RESTRICTIONS?

A. It is unclear. On page 44 of his direct testimony, Mr. Filarowicz identifies "SWEPCO Credit Ratings and Dividends" as his first recommendation, but the following description provides no mention of dividends. Thus, it is unclear whether Staff recommends dividend restrictions if SWEPCO's credit ratings fall below current levels.

Q. SHOULD THERE BE FURTHER RESTRICTIONS ON DIVIDENDS?

A. No. The Company has a long history of making reasonable and reasoned dividend decisions for the benefit of SWEPCO and its customers. With no prompting from the Commission, SWEPCO has not paid a dividend since 2019 in order to support the capital program and credit ratings. The Company has been an exceptional steward of the credit ratings and capital for the benefit of SWEPCO customers. Placing unnecessary dividend restrictions on SWEPCO at this time disregards that history.

Q. HAS AEP FURTHER DEMONSTRATED A COMMITMENT TO SWEPCO'S CREDIT QUALITY?

A. Yes. In addition to the dividend holiday described above, AEP has recently supported the Company with equity contributions totaling $175 million in order to help maintain SWEPCO's credit ratings.

Q. WOULD DIVIDEND RESTRICTIONS CHANGE EQUITY CONTRIBUTION DECISIONS FOR SWEPCO?

A. Yes. It would change how SWEPCO and AEP evaluate both dividends and capital contributions. Currently, the Company can make dividend and equity contribution recommendations with the understanding that capital can be returned to the parent as a dividend when cash flows are available to support a dividend. Commission imposed dividend restrictions would increase risk for AEP and may deter future equity contributions.

Q. HAS SWEPCO BENEFITTED RECENTLY FROM BEING PART OF THE AEP FAMILY?

A. Yes. The recent winter storms in the Southwest caused extraordinary natural gas and purchased power bills that SWEPCO had to pay almost immediately. SWEPCO was able to rely on AEP to provide equity while waiting to come out of blackout (issue financial statements) and issue additional bonds. SWEPCO benefited from being able to manage the capital needs without undue restrictions.

Q. WERE DIVIDEND RESTRICTIONS REJECTED BY THE COMMISSION IN DOCKET NO. 49494, WHICH INVOLVED SWEPCO'S SISTER COMPANY, AEP TEXAS?

A. Yes. The Proposal for Decision in Docket No. 49494 recommended that the Commission **not** adopt dividend restrictions and seven other ring-fencing measures proposed by Staff in that case.[3] After the issuance of the Proposal for Decision, the

[3] *See* Application of AEP Texas Inc. for Authority to Change Rates, Docket No. 49494, Proposal for Decision at pages 163-164 (November 12, 2019).

parties in Docket No. 49494 submitted an unopposed agreement for Commission approval, but left open the issue of dividend restrictions. At its February 27, 2020 open meeting, the Commission evaluated the settlement agreement and voted to approve it without imposing dividend restrictions on AEP Texas.[4]

Q. SHOULD THIS COMMISSION PRECEDENT APPLY TO SWEPCO?

A. Yes. SWEPCO is similarly situated and shares the same parent company as AEP Texas.

Q. DID THE SETTLEMENT AGREEMENT IN DOCKET NO. 49494 ADDRESS ANY OTHER RING-FENCING MEASURES?

A. Yes. The parties' agreement regarding ring-fencing measures was adopted as Findings of Fact Nos. 109 through 120 in the Final Order in Docket No. 49494.[5]

Q. WOULD SWEPCO CONSIDER SIMILAR RING-FENCING MEASURES IN THIS CASE?

A. Yes. SWEPCO is already abiding by most of these measures.

Q. DOES STAFF PROPOSE ANY OTHER RING-FENCING MEASURES THAT ARE UNACCEPTABLE TO THE COMPANY?

A. Yes. Staff's second recommendation that SWEPCO must notify the Commission if its standalone rating or AEP's rating falls below investment grade is unnecessary. If SWEPCO's rating falls below investment grade, that information will be made public. Also, Staff's third recommendation that SWEPCO agree not to seek a higher ROE if its credit ratings fall below investment grade is unacceptable. There are many different

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[4] *See* Docket No. 49494, Final Order at page 2, and Finding of Fact Nos. 108 through 121 (April 6, 2020).
[5] *Id.*

variables and unknowns about what would precipitate a below investment grade rating, that it would be imprudent and unreasonable for SWEPCO to make such a commitment. Staff's fifth and sixth recommendations regarding no cross-default provisions and rating agency triggers relating to affiliates are likewise unnecessary and would increase compliance costs for customers. SWEPCO issues its own debt based on its own standalone credit rating.

Q. DO YOU AGREE WITH STAFF'S RING-FENCING RECOMMENDATION NO. 13 (NO INTER-COMPANY LENDING AND BORROWING COMMITMENT)?

A. No. Although Staff rightly excludes the utility money pool from this recommendation, it is still too restrictive and inefficient. There are other inter-company lending and borrowing programs that could be used by SWEPCO under the right circumstances. The wholesale prohibition on this lending is unreasonable. Affiliate long-term notes have been issued by various utilities to AEP, which has enabled the utility to forgo all of the normal debt issuance costs and still access needed capital in a timely manner and in fact this could have been necessary for SWEPCO due to the recent winter storm. It would be unusual for SWEPCO to do this, but it should still be available. Moreover, the Federal Energy Regulatory Commission (FERC) also allows a utility to open account advances, if funding is needed beyond its short-term debt authorization limit. FERC basically allows a utility's parent to issue a no interest loan to its subsidiary. It would be a benefit to both SWEPCO and its customers to maintain access to this low cost liquidity option.

Q. DOES THIS CONCLUDE YOUR REBUTTAL TESTIMONY?

A. Yes, it does.